Message from State Controller
Kathleen Connell

The United States will soon see its largest senior population in history, as baby boomers begin to retire this decade. As a whole, baby boomers are more numerous, more educated, and more affluent than any segment of the U.S. population has ever been. Their influence has transformed our society, our economy and our public policy. As they enter their golden years, they will transform our retirement system in a way that will affect all future generations. This edition of the *Controller's Quarterly Report* explores the challenges of retirement, and the baby boomers surface as a recurring theme.

The report begins with an examination of the economic uncertainty we face as this generation of 76 million people approaches retirement. As the baby boomers prepare to retire, the economy is weakening, both in the U.S. and in California. Job growth has leveled off, threatening a recession, and the nation is reeling from the impact of terrorist attacks on New York City and Washington, D.C. The attacks will further strain both the national and the California economies and the U.S. response will divert precious resources. Extensive planning and development to meet the health-care and economic needs of this large wave of seniors is required.

The unique demographics of the baby boomers, combined with their retirement patterns and other economic and social factors, are creating a more complex retirement picture that will need to be addressed by policy makers, professionals and individuals.

When the boomers retire, the workforce will never be the same. The unique characteristics of this generation have made them a tremendous asset in the workforce. "Public Employees: Aging, Educated and Retiring Early" discusses the traits of the boomers that make them so valuable to the workforce, and more specifically to State government. A change in California law that allows State employees to retire earlier means that baby boomers, already hard to replace, will now leave sooner and in larger numbers.

The tidal wave of retirement will strain the Social Security Trust Fund. Social Security reform is a hot-button issue that this *Controller's Quarterly Report* explores in depth. Alternative projections for the fund are explored in "Productivity Growth and Social Security." A critical look at reform, "Should We Privatize Social Security?" follows delineating the issues that must be addressed in order to privatize Social Security.

For nearly all retirees and their families, long-term care is an area of concern. Our system fails to deliver long-term care to those who need it, unless they are in poverty. That is the subject of "Long-Term Care." Of particular concern is the fact that people of this generation are less likely to have family members who can care for them as they age.

Retirement is especially difficult for women and, in this regard, the baby boom generation has not made many advances. Despite an increased presence in the workforce, the women of the baby boom generation are still lagging behind their male counterparts when it comes to wages, pensions and other retirement resources. The article "Women's Retirement Security" proposes some solutions.

Finally, another consideration is determining how a growing senior population will impact the system. The demand for services will increase. The question is which regions will see the greatest change? The demographics of the aging are analyzed in the "Local Aspects of an Aging America."

We call retirement "the Golden Years" for a reason. It is supposed to be a time of rest and leisure following a lifetime of work. However, many of these factors may cast a shadow on this happy image, if not for baby boomers, then for the generations that follow them.

As Chief Financial Officer of the State of California and as a board member of the State's two largest retirement systems, CalPERS and CalSTRS, I see a critical need to identify solutions. The events of September 11 will undoubtedly lead to an increase in defense spending, security precautions, and a possible airline industry bailout. While these economic hardships will certainly have an immediate effect, we cannot allow our attention to be diverted from planning for the care of our elderly population.

KATHLEEN CONNELL
Controller, State of California

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The California Economy: Autumn Update

> **"The September 11 attack will almost certainly cause further deterioration in consumer confidence."**

A World on Hold

Economic outlooks are generally produced by observing trends and projecting those trends with the guidance of historical precedents. On September 11, the nation witnessed an event without historic precedent. The September 11 terrorist attacks on New York City and Washington, D.C., killed more people than did the attack on Pearl Harbor and the bombings of the World Trade Center (in 1993) and the Oklahoma City bombing combined. They occurred on U.S. soil and disrupted global commerce. It will be months before the impact of this event can be assessed. At this writing only a few days of observations guide us.

On September 11 stock markets around the world sank, but the quick and decisive response of central banks restored calm the next day. The Federal Reserve and central banks around the world responded quickly to assure that global markets would have the liquidity to function in both the near and longer terms.

Recent U.S. Economic Evidence

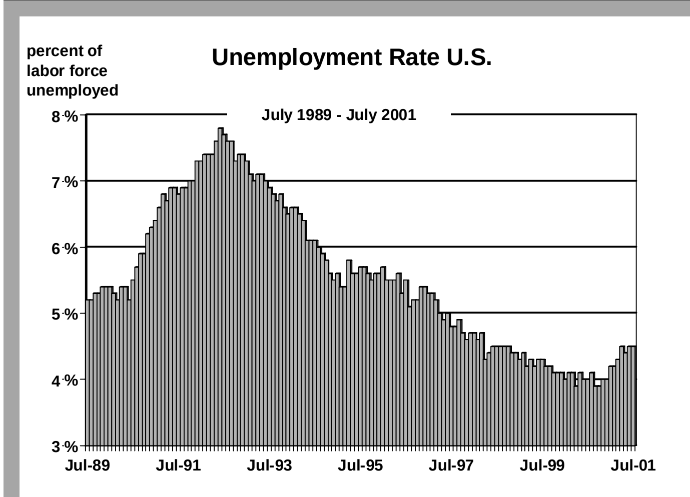
Prior to the September 11 attack the Federal Reserve had instituted seven interest rate reductions totaling 300 basis points during the first eight months of 2001. The impact of the Fed's moves to reduce the cost of borrowing should be hitting with full force now, just as the tax rebates inject extra funds into household wallets. On September 17, an hour before the reopening of the New York Stock Exchange, the Fed moved to cut both the federal funds rate and the discount rate by another 50 basis points, and the expectation is that we may see more cuts before the end of the year.

Business investment has been in a sharp decline throughout the year. Consumer spending on retail goods and services is soft. In the second quarter of 2001, real consumer expenditures grew by only 2.2 %, but it was enough to produce positive, albeit scant, growth in real GDP. However, this is the first time spending growth has slipped below 3% since 1996. The University of Michigan reported that consumer sentiment in early September took a sudden dip to its lowest level since 1992. The September 11 attack will almost certainly cause further deterioration in consumer confidence.

Against expectations, gas prices failed to skyrocket this summer and actually moderated. Additionally, the IRS is now distributing $40 billion in tax refunds and wage earners are taking home slightly bigger paychecks. It is hoped that the extra cash that households are finding in their pockets will buoy spending in the coming months.

Signs of a strengthening economy started to trickle in during July and August, though overall the picture is still mixed. The U.S. leading indicators index rose again in July for the fourth month in a row. New claims for unemployment insurance peaked in July and appeared to

Figure 1



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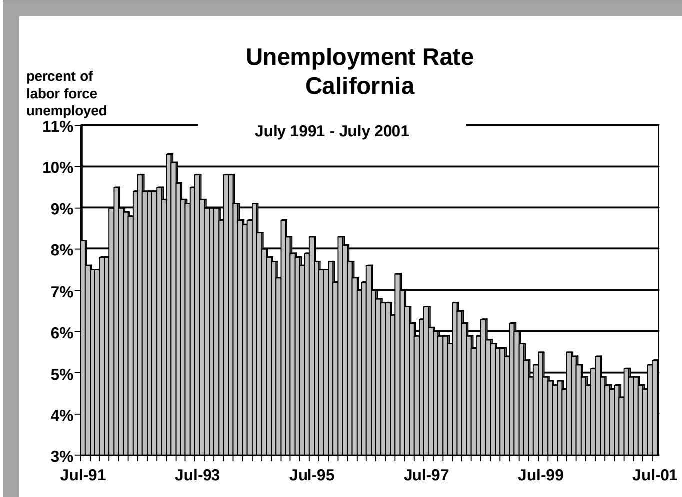

be drifting lower until early September when they began to climb. Workers who lose their jobs appear to be having trouble finding new ones, driving the number of people collecting benefits to their highest level since August 1992. Automobile sales and housing starts have remained strong all year, and home sales have yet to weaken. The unemployment rate in the U.S. has risen from a low of 3.9% in October 2000 to its current level of 4.9%, still low by historical standards. A lagging indicator, unemployment rates usually rise toward the end of a business cycle. Prior to September 11, there was reason to believe the weakest part of the economic downturn was behind us. In the short term, a rise in unemployment is expected. Insurance, tourism and the airline industry have been hard hit by the events of September 11 and employment will undoubtedly decline as a result.

A Cool California

The summer of 2001 was cool and that reduced the demand for power and the need for peak electricity generation in California. Hence, no brownouts or blackouts occurred in the State during its most vulnerable season. Voluntary conservation by consumers and businesses also helped to reduce the demand for electricity and avoid the possibility of blackouts. Consequently, the energy crisis has been relatively tame since the spring. Going forward, the power shortage issue should diminish in importance as new plant capacity comes online over the next two years.

Employment Trends

The California tourism industry, however, will suffer a contraction over the next several weeks and possibly longer. California is the number one tourist destination in the nation — for both domestic and foreign travelers. With a strengthened safety system, however, this hopefully will be a transitory contraction.

The Sacramento Valley and Southern California economies are not reeling from the information technology fallout that the Bay Area is now experiencing. Unemployment rates remain at historical lows in these regions and business activity is still relatively vibrant. Nevertheless, economic growth has cooled in the State, especially during the second and third quarters. However, this was expected in view of the unsustainable pace by which many statewide economic indicators were growing. A return to moderation was expected from the hyper-growth that characterized the State's economy between 1997 and 2000.

Interest Rates, Refinancing, and Home Sales

The eight interest rate reductions this year by the Federal Reserve have dropped the Federal Funds rate to 3%, the lowest level since 1994. Until recently, the rate reductions have had little direct effect on mortgage rates, which remained relatively steady for most of the year. In recent weeks, however, mortgage rates have fallen again due to new buying of 10- and 30-year Treasury bonds in the financial markets.

In early September, the yield on 30-year Treasury bonds declined to 5.35%, the lowest level since 1997. Mortgage rates have fallen in tandem with treasury yields. Fixed rate mortgages are well under 7%, and adjustable rate mortgages are now below 6%.

Low mortgage rates are keeping home sales near record levels, and refinancing activity

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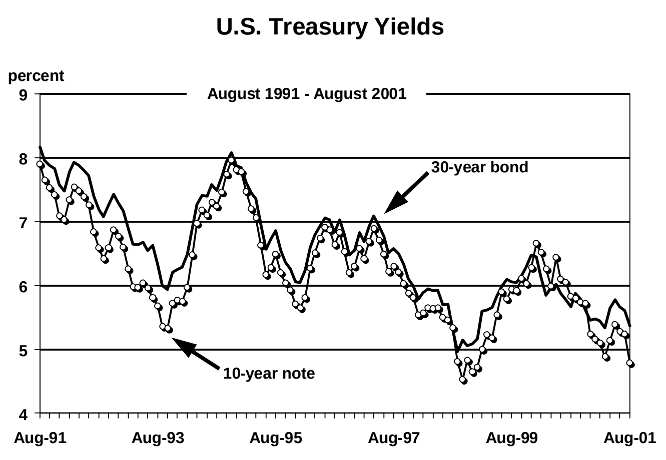
Figure 3



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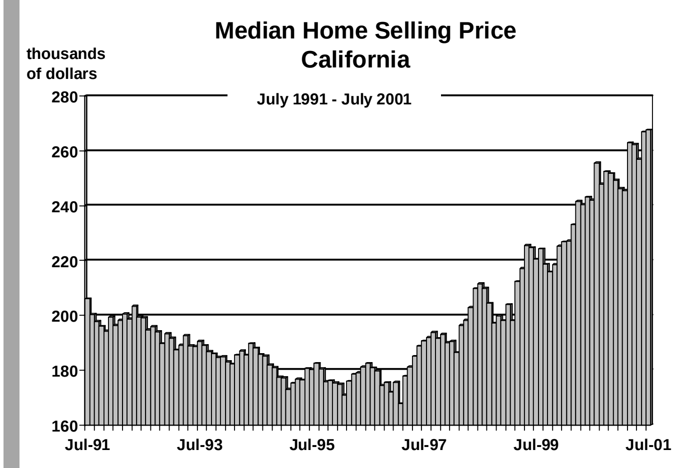

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is strong, offsetting some of the other weaknesses in consumer spending. It is estimated that homeowners have saved $35 billion in extra cash by refinancing during the first six months of this year. In the first quarter alone, refinancing activity contributed to nearly half of the 1.3% annualized growth in real GDP.

Refinancing activity continues to be strong, bolstered by low mortgage interest rates, strong house price appreciation, and heavy marketing by lenders. Indeed, after slowing since April, the weekly Mortgage Banker's index of refinance applications has risen steadily for the last six weeks and remains substantially higher than year-ago levels.

Home sales in 2001 are off the record pace set in 2000, but here again, a cool-down was expected. Home buyers are on pace to buy 506,000 homes this year in the State, 7.5% lower than last year but still above the home selling rate in 1998. Selling prices have advanced to record levels this year, up another 9% over year 2000 median home prices.

California Employment

The rapid rate of employment growth in the State has cooled. As evidence, the August year-over-year job growth has slowed to 1.3%. Consequently, the unemployment rate rose in August to 5.2%, a slightly higher rate than year-ago levels.

During the past 12 months, the State created 194,600 new non-farm jobs. The principal industries adding jobs include the following sectors:

Services	82,200
State/Local Govt.	81,800
Wholesale and Retail Trade	47,500
Construction	23,100
Finance and Real Estate	18,300

The manufacturing sector has shed the most jobs in the past twelve months — 51,200 — concentrated mostly in metal work, industrial machinery (including computers), and electronic equipment.

Between January and August 2001, dot-coms trimmed 87,795 jobs in the U.S., more than twice as many as in 2000, which saw a total of 41,515 pink slips. The California experience of dot-com tragedies is in line with national numbers, but many of these workers have apparently been re-hired, or were never actually let go. That is a principal reason why job growth remains positive in California this year.

"The California experience of dot-com tragedies is in line with national numbers, but many of these workers have apparently been re-hired, or were never actually let go."

Last year, total employment rose 3.8%, the largest gain in 17 years. This year, the outlook calls for a noticeable slowdown in job creation. Prior to the events of September 11, job creation in California had been expected to slow to 2.1%. Since California has a large tourist industry that will be affected by a reduction in discretionary travel, job growth is likely to be much lower, perhaps under 1%.

The rate of unemployment is expected to rise in California during the autumn months. There may be a sharp rise in unemployment over the next month or two, but at least some of that rise will be transitory as the travel industry returns to a more normal level, hopefully by the holiday travel season.

Some layoff announcements do not necessarily result in the same number of employees let go. Conditions may turnaround for the company sooner than expected. Furthermore, many workers are hired back quickly, either by the same firm or by competing firms in the industry. This may explain the behavior of the unemployment rate in California, which hit a 32-year low in July.

Personal Income

Last year, personal income jumped 11.5%. Income from all assets, including financial assets, grew by nearly 8%. This year has seen far fewer capital gains from stock market sales. Wage and salary income growth is being limited by moderate labor market growth, and the extent of corporate income gains is weakened by the softening U.S. and state economies.

During the first six months of 2001, personal income improved 3.8% over year-ago levels. This is a significant slowdown compared to the nearly "double-digit" growth in income during 2000.

Adjusted for inflation, per capita personal income has been flat this calendar year, showing no discernable growth. However, this is not alarming in view of the unsustainable gains that real per capita incomes experienced in California from 1998 through 2000. Though capital gains income will be soft in 2001 and 2002, continued labor market strength in the State will produce more wage and salary income, the largest component of personal income.

Personal income tax receipts, the largest single source of revenue to the California General Fund, leaped 14% for the fiscal year ending June 30, 2001. Income tax receipts are expected to increase 5% to 7% during 2001-02.

New Development

Home builders have remained very busy in California during 2001, especially in the Santa Clarita Valley of Los Angeles County, San Joaquin County, and the Sacramento Valley (including Placer and El Dorado Counties).

For the first seven months of 2001, the annual pace of new home permits is averaging 151,000, a slight increase of 3,500 units over last year's level. The outlook does not forecast a significant softening in this sector, because of the chronic excess demand for housing in the State. The demand for housing, particularly in the coastal communities, is not being met with adequate supply. Consequently the housing affordability problem continues to escalate.

Office vacancy remains low in most areas of the State, but rates have moved up noticeably in Santa Clara County and the Bay Area. Commercial vacancies in Southern California have softened, but have not changed significantly, especially in Ventura, San Diego, and Orange Counties.

New commercial development is also ahead of last year's pace, by 34%. More commercial buildings are currently underway in the Central Valley, Santa Clara County, the Sacramento Valley, and the Inland Empire.

The General Outlook

September and October may show a decline in consumer spending. With unprecedented interest rate reductions by the Federal Reserve totaling 350 basis points this year and still low rates of unemployment, consumers are not likely to curtail their spending significantly for a prolonged period of time. To date, the weaker economy has had very little effect on consumer purchases of real estate and automobiles.

The information technology breakdown, combined with the electric power crisis, foretold a rough economic ride for the State during the second half of 2001. However, electric power was seemingly plentiful during the summer months, and the IT problems appear to be correcting themselves faster than anticipated, through layoffs and rapid inventory adjustment.

Southern California will produce the most jobs in the State this year, principally from Ventura, Orange, and the Inland Empire Counties. Job growth in the Sacramento Valley will also remain strong for the rest of the year.

Home builders are currently busy, trying to meet the demand for housing in the State. New housing production will continue through 2001 and 2002. Affordability is still a problem in most coastal areas, but very low interest rates are helping to make housing slightly more attainable.

We believe that the next two months will see a small contraction in employment, followed by a return to slow growth near the end of the year. ❖

"Home builders are currently busy, trying to meet the demand for housing in the State."

Controller's Economic Council: Forecasts for 2001

August 2001

Council Member Organization	Representative	Employment growth (percent)	Unemployment Rate (percent)	Personal Income Growth (percent)	Residential Building Permits (in thousands)
California Association of REALTORS©	Robert Kleinhenz	2.0	5.2	5.4	152
California Economic Forecast	Mark Schniepp	2.0	5.3	5.2	151
LA County Economic Development Corp	Jack Kyser	1.9	5.4	2.2	134
The Milken Institute	Ross DeVol	1.9	5.2	4.6	148
Munroe Consulting	Tapan Munroe	1.5	5.5	5.3	140
UC Berkeley, Center for RE & Urban Econ	Cynthia Kroll	1.7	5.4	3.5	135
UCLA Anderson Forecast	Tom Lieser	1.8	5.2	5.6	157
Mean		1.8	5.3	4.5	145
Median		1.9	5.3	5.2	148
State Controller		0.9	5.5	4.5	150
Actual Values for Calendar 2000		3.8	4.9	11.5	148

Source: State Controller's Office: Council of Economic Advisors

Public Employees: Educated, Aging and Retiring Early

> **"Government jobs in general are highly concentrated in white collar occupations, and thus more likely to require a college education."**

The workforce in California is aging and in no sector of the economy is that more apparent than in the public sector. To look at what this means for the governments of the State we begin with an examination of the demographic characteristics of the California workforce in the public and private sectors. This report focuses on the population aged 25-64. People in this prime working age have typically completed their education and are launched into their careers.

This report is in two sections. Data used in Figures 1-6 and Tables 1-2 comes from the 1999 and 2000 Current Population Surveys (CPS), March Demographic Sample. The two years of CPS data were combined to increase the sample size and hence the reliability of this small survey. The combined files give an effective date for the data of about September 1999. The CPS data allows a comparison of public (State & Local government) and private-sector workers as well as a comparison of California with other states. The public-sector employees included in this data are employees of the State, counties, cities, school districts, and other local agencies.

The final section of the report provides a detailed look at retirement trends in two specific public sector agencies: State government and California State University (CSU) employees. The data we examine are summary statistics compiled from employee records for those two entities.

Public and Private Sector Employees in California

An Older Workforce

Figure 1 compares the age distribution of state and local government employees aged 25-64 to that of employees in the private sector. Employees of state and local government in California have much higher concentrations of employees aged over 45 than does private industry.

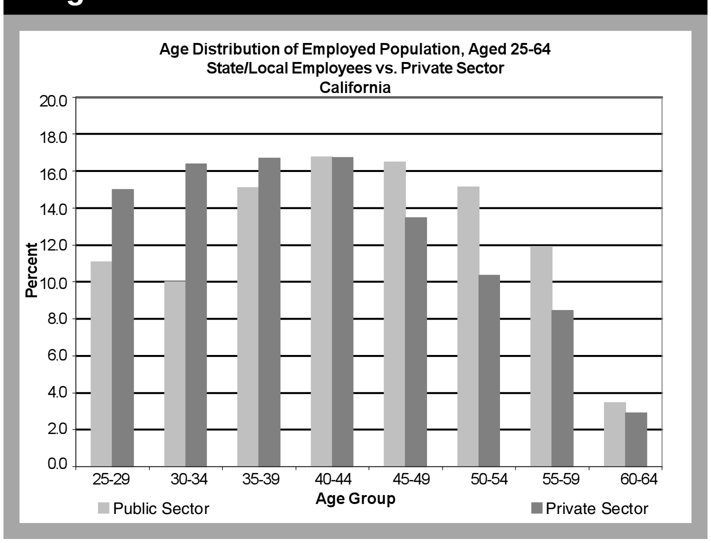
Figure 2 shows the same age distribution for the rest of the U.S. The age pattern of public- and private-sector employees for the U.S. is quite similar to that of California.

An Educated Workforce

Another distinctive feature of the public-sector workforce in California is the education profile. Figure 3 shows the distribution of educational attainment of employees in the public and private sectors of the California workforce. The state/local sector has a much higher proportion of workers with a college education. One reason for this is the large numbers of teachers in the state/local sector—all of whom have a college degree. It is also the case, however, that government jobs in general are highly concentrated in white collar occupations, and thus more likely to require a college education. California does not differ significantly in this respect from the rest of the U.S. (Figure 4).

The most significant difference in distribution of California workers compared to the rest of the U.S. is in the percentage of the private

Figure 1



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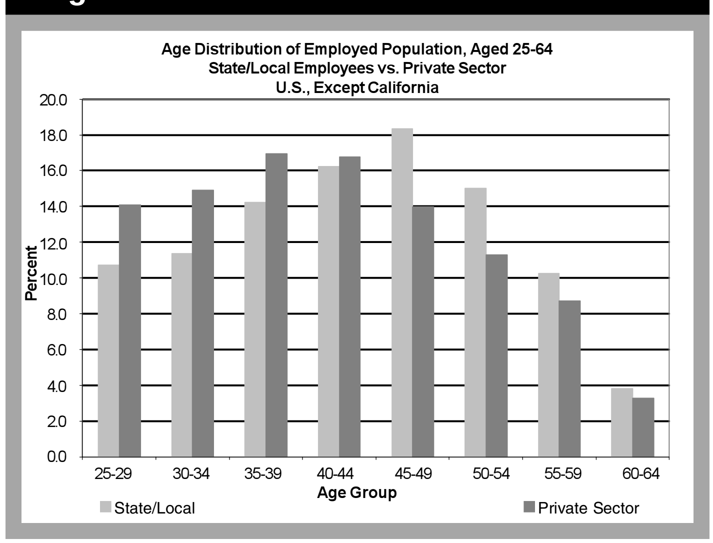


workforce that has less than a high school education. In California, workers without a high school diploma represent over 17% of private-sector workers, while only 10.5% of private-sector workers in the rest of the U.S have not completed high school. The education factor is even more important if we look at the distribution of education by age.

Figure 5 depicts the distribution by age of the California population that has completed college and the percentage that has not completed high school. Clearly the best-educated segment of the population in California is the leading edge of the baby boom generation (those aged 45-54). By contrast, the population under age 35 has fewer college graduates and more people who have not completed high school. Since public agencies have a large need for college-educated workers and very few jobs for those who have not completed high school, this will make replacing the baby boomers a greater challenge in California than in other states.

Figure 6 shows the same data for the four largest states (other than California). While these other large urban states also have their highest educated workers concentrated in the 45-54 year group, the disparity between the workers approaching retirement with the youngest workers is not as great as it is in California. When California's baby boomers retire, government agencies will face considerable competition for college-educated workers in the job market.

A Trend Toward Early Retirement

The age at which workers retire has been trending downward for the last 40 years. This is the result of the availability of retirement plans and social security, the combination of which have made a comfortable retirement at an earlier age possible. In the early 1950s the median age of retirement was just over 67 years. The Social Security Administration reports that the mean age of persons initially awarded Social Security benefits in the year 2000 was 63.6 years. The Bureau of Labor Statistics has projected that the mean retirement age for all workers in the period 2000-05 will be about 61.5 years.

Contributing to the challenge for State and local governments is the reality that government employees tend to retire early. The two biggest public pension funds in California are the California Public Employees' Retirement System (CALPERS) and the California State Teachers Retirement System (CALSTRS). The average age of retirement for members of these two systems in the year 2000 was just over 60 years. This indicates that state and local governments are likely to see baby boom retirement waves begin earlier than in the private sector. The leading edge of the baby boom generation will turn 60 in 2006.

A comparison of the age and income of public-service retirees to private-industry retirees using the CPS confirms the earlier retirement of public employees. The CPS asks whether the respondent has any pension income. If the answer is "yes," the respondent is asked

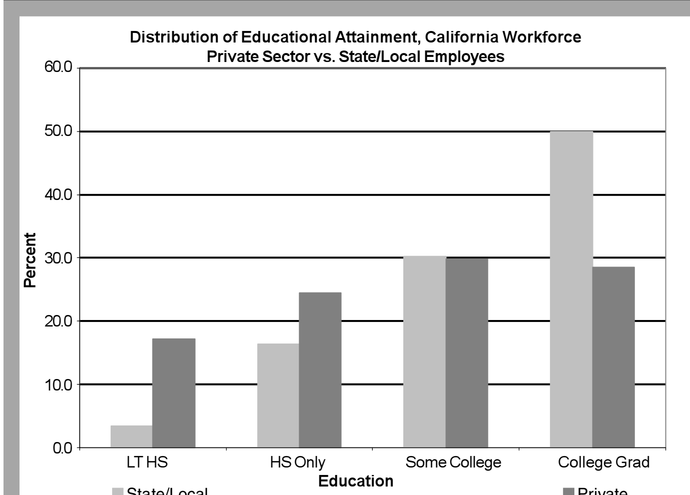
"When California's baby boomers retire, government agencies will face considerable competition for college-educated workers in the job market."

Table 1

Age Distribution of California Retirees Who Have Pension Income By Sector

Sector	45-54	55-64	65+
Private Industry	3.0%	17.8%	79.2%
State & Local Government	2.0%	25.9%	72.1%

Figure 3



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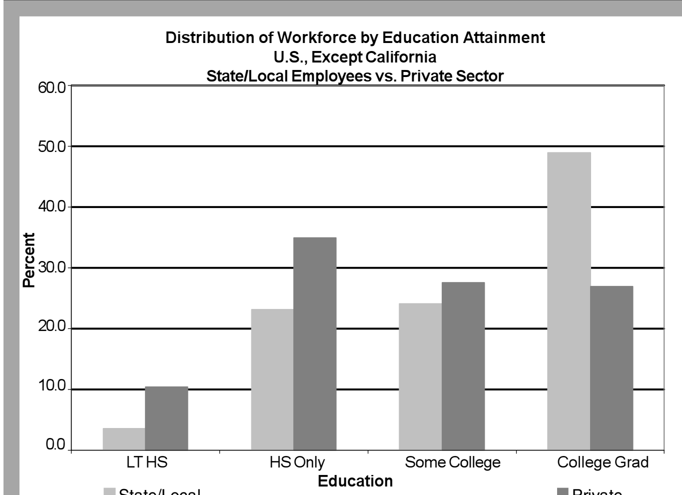

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the source of that pension income. Table 1 shows the distribution by age of retirees who had pension income from either a private company or from a state or local government agency. While the CPS does not give us the age at which the respondents retired, the data shows that 26% of public-sector retirees are in the 55-64 year age group, compared to only 18% of private-sector employees.

One reason that public employees retire earlier is because they are more likely to have pension coverage. Almost 80% of all workers in the public sector are covered by a pension plan (employees excluded in the public sector are primarily consultants, part time and temporary employees). By contrast only about half of employees in the private sector are covered by a pension plan. Private firms provide jobs for almost 70% of the workforce. Only 17% of the self-employed (about 12% of the workforce) have pension coverage.

It also appears that the pension coverage of public employees gives higher income benefits. Table 2 shows the income distribution of retirees in the public and private sector for those who receive pension benefits. The last column in Table 2 shows the income distribution of retirees in the private sector if we add to the private sector those retirees who say they have no pension benefits (other than Social Security). These data cover income for individuals; household incomes of these retirees may be considerably higher.

"One reason that public employees retire earlier is because they are more likely to have pension coverage. Almost 80% of all workers in the public sector are covered by a pension plan."

Table 2

Income Distribution of California Retirees in the Public (State and Local Government) and Private Sectors

Income	State & Local Government	Private Sector	
		W Pension	W&WO Pension
$0-19.9K	25.7%	41.0%	71.2%
$20-39.9K	37.9	33.9	16.5
$40-59.9K	17.8	11.7	5.5
$60K+	18.5	13.4	6.8

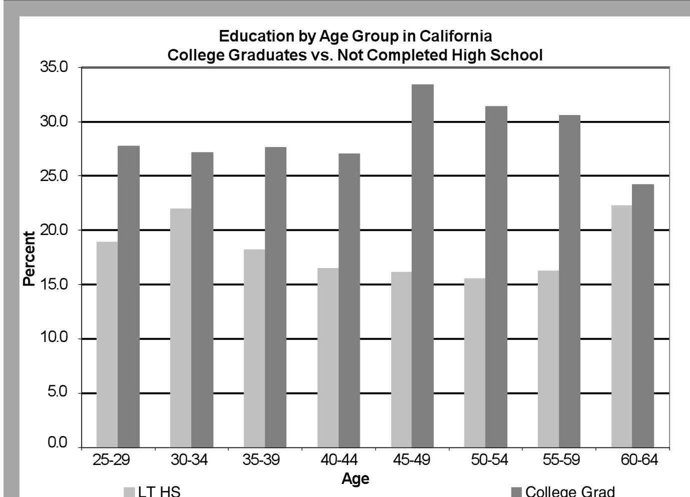
When Will the Wave Hit?

In this section we examine in detail the retirement trends for a subset of public employees: State employees and employees of the CSU system. The data used in this section is not a sample but rather summary statistics on full-time workers compiled from the employee files of these two systems.

The oldest baby boomers turn 55 this year, an age at which many workers begin to think of retirement. In California, workers aged 50-54 represent 11.2% of the employed population in the prime working years of 25-64. But for full-time state government workers, the figure is 17.1% and for California State University employees that single five-year cohort represents almost 20% of prime working-age employees. Many of these older workers are highly skilled and hold key positions. The State and the CSU system are thus faced with a large cohort of valuable workers approaching retirement.

A key to when workers choose to retire is the type of retirement plan that covers the worker. Retirement plans for public employees in the California are run by 62 publicly administered retirement funds and an array of privately administered funds (such as police union funds). Virtually all public employee retirement systems are "defined benefit" systems. Under a defined benefit system the member and the employer contribute to the system based on a percentage

Figure 5



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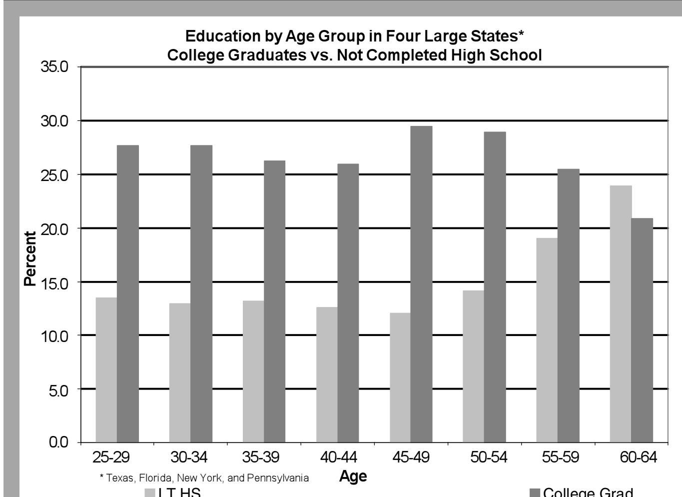


of the member's salary. Retirement benefits are typically based on the average of the highest earnings of the employee, the employee's age, and years of service. These systems often have a cap of benefits that kicks in at or before age 65. This tends to encourage early retirement in defined benefit systems. Some employers have used this as a way to regulate the size of their workforce. Employers offer retirement incentives by crediting members that are near retirement with additional years of service. These older workers are often highly paid and the tactic shifts the cost of these employees from the company payroll to the retirement fund.

Thirty years ago the majority of both public and private employers offered defined benefit plans. Now only 22% of employees in the private sector are covered by defined benefit plans. The majority of retirement plans offered to newly hired workers in the private sector are called "defined contribution" plans. An example of a defined contribution plan is a 401(k) plan. Under this plan a worker and his employer both contribute to a fund, but the benefits available to the worker on retirement are determined by the amount of money contributed and the success of the fund's investment—there is no specified benefit amount guaranteed on retirement. Many employees that have a defined benefit plan, including many government workers, also have a defined contribution plan.

The prevalence of defined benefit plans increases the percentage of public employees who retire younger. This may drop even lower over the next few years. In late 1999 the California Legislature passed an amendment (SB400) to the Public Employees Retirement Law that is likely to accelerate early retirements among California public employees. One of the provisions of the bill changed the salary on which retirement benefits are based from the highest three years of salary to the highest 12 consecutive months. In addition SB400 allowed the same formula to be used for those employees that retired at age 55 as previously used for those who retired at age 60. This bill became law in January 2000; Figure 7 shows the effect of this bill on retirements of state employees.

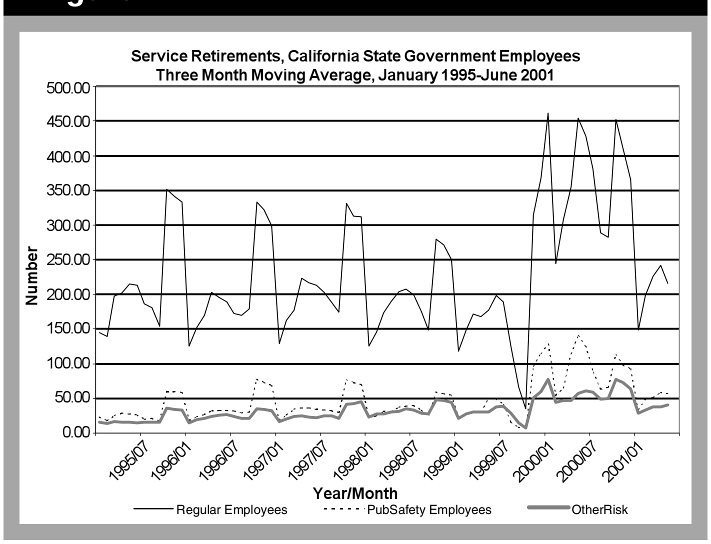
Before 1999 there is no clear trend in the number of applications for retirement. A pronounced surge of retirements began in 2000, but in 2001 the number of retirements seem to drop back closer to their pre-SB400 levels. The surge in 2000 probably reflects some accelerated retirements but likely included some employees who would have retired in 1999 but found it more beneficial to wait until 2000. Also there seems to have been a concurrent decline in disability retirements (Figure 8), indicating that some of these service retirements were in place of disability retirements.

Figure 9 shows the service retirements and disability retirements for CSU employees. CSU retirements show a large jump in 2000, but unlike the subsequent drop seen in the State system, it appears that CSU retirements in 2001 are far ahead of previous years.

A detailed age profile of workers in these two systems shows that a large number of workers will reach the magic age of 55 this year, and the numbers will be high for the next ten years. Figure 10 shows the age distribution of state workers by single year of age for workers between 35 and 65. Figure 11, displaying the same data for CSU employees, shows even higher

"The prevalence of defined benefit plans increases the percentage of public employees who retire younger."

Figure 7



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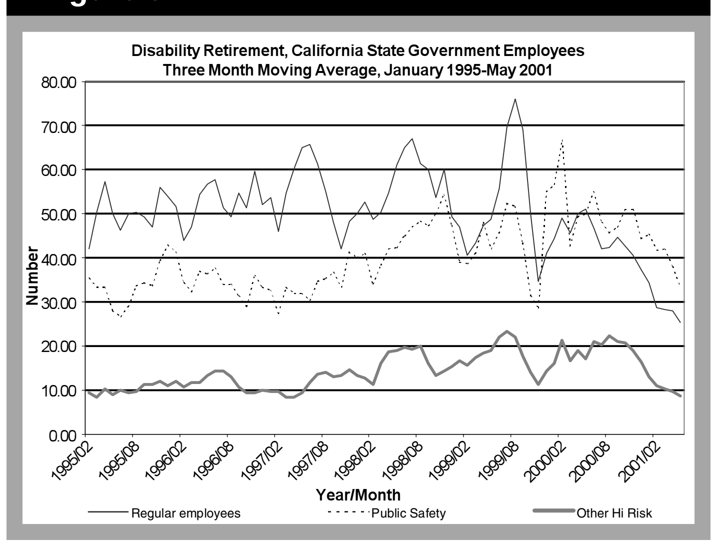

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concentrations of employees nearing retirement than does the state employee profile, which probably explains the continuing rise in CSU retirements. The pronounced drop between employees aged 55 and 56 in both charts probably reflects not only the baby boom cohort but also the effect of prior early retirements and disabilities in the workforce older than 55.

Clearly, there is likely to be a pronounced rise in retirements as this large cohort passes through the retirement gate that has now been lowered to age 55. Although the data on state employee retirements does not reflect a large increase so far this year, the surge does appear to be underway in the CSU system. The wave has arrived on our shore.

"California will see the first waves of baby boomers retire before the end of this decade."

Summary

California will see the first waves of baby boomers retire before the end of this decade—the result of the convergence of an aging boomer generation and a declining retirement age . State and local governments are likely to see retirement waves even earlier. The CSU system is probably already entering the retirement surge, with other agencies not far behind. The problem for those public agencies will not be just finding workers, but in finding workers with the skills to fill the jobs of government. ❖

Figure 9

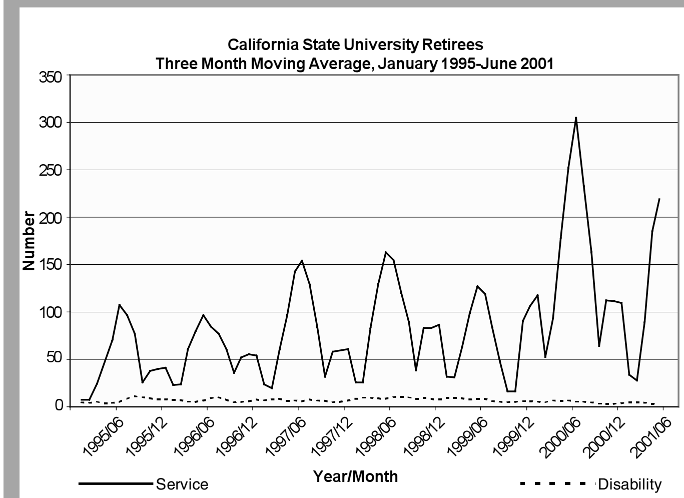


Figure 10

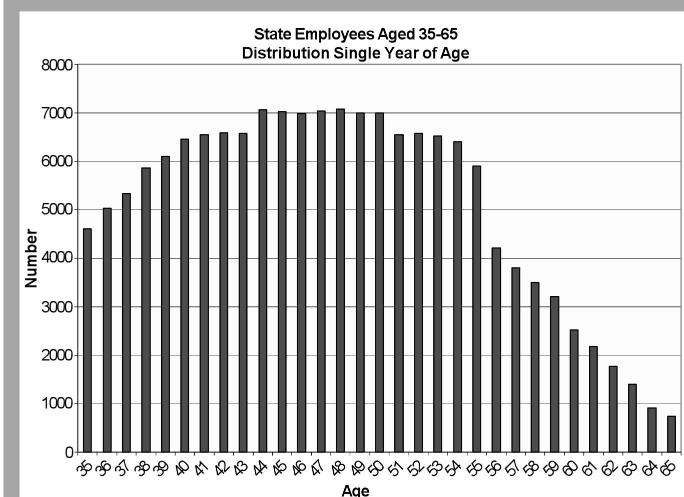
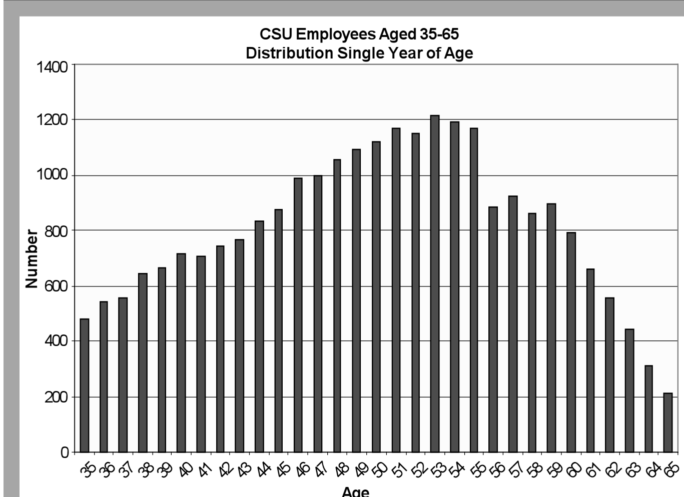
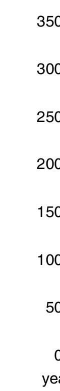
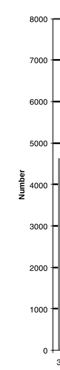


Figure 11







Productivity Growth and Social Security

By
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Social Security reform has again become a hotly debated issue in the political arena. President George W. Bush made Social Security one of his central issues during the election campaign last year, and his administration has followed up by establishing the presidential Commission to Strengthen Social Security this spring.

The presumed need for Social Security reform stems from a predicted shortfall in revenues in the relatively distant future. According to the Social Security trustees, payroll taxes will exceed promised benefits until 2016. From 2016 to 2024, Social Security is expected to cover any shortfall in tax revenue from the interest it earns on its assets. In the meantime, Social Security will continue to build up its trust fund to the tune of $3.3 trillion in today's dollars. After 2024, Social Security is projected to cover any expected shortfall by selling off its assets until they are gone in 2038. Beyond 2038, Social Security's income is forecast to cover about 70% of promised benefits if nothing changes.

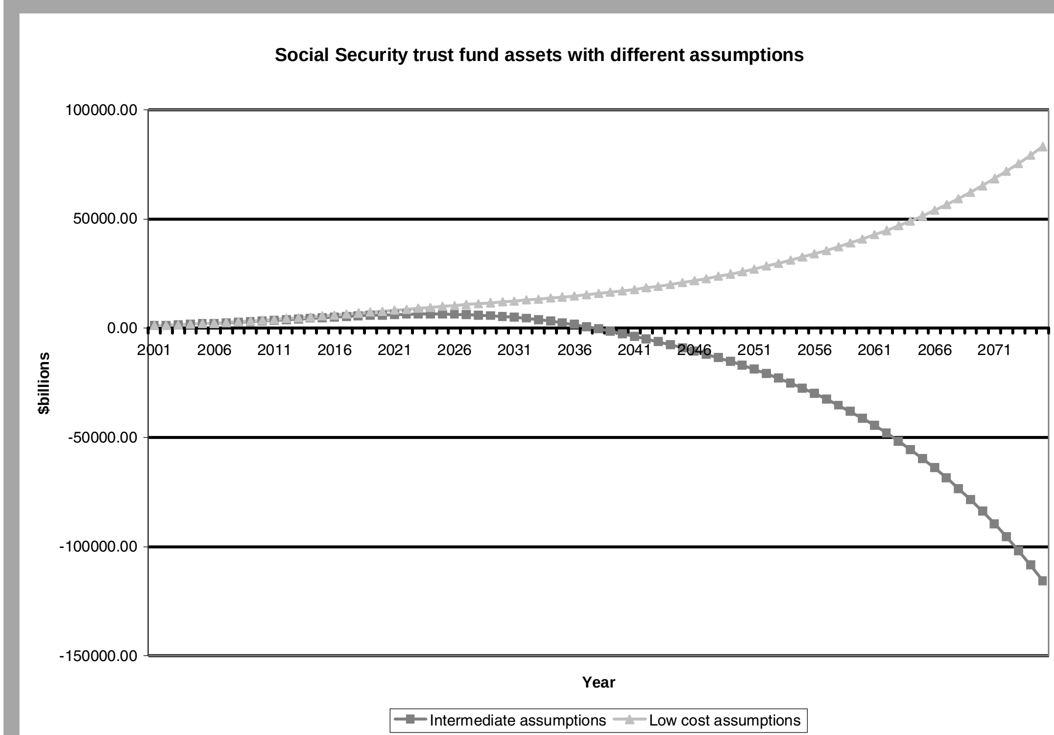
The anticipated shortfall in 2038 and thereafter hinges on a particular set of economic and demographic assumptions. The trustees have generated three different sets of assumptions: those that are generally used, which show a shortfall in 2038; one that is more pessimistic than this; and one that is more optimistic.

Even though nobody can accurately forecast the future, there is a good reason why the trustees' middle-of-the-road or "intermediate" scenario is likely too pessimistic. The forecasts for Social Security rely heavily on assumptions about productivity growth, which the trustees project will grow at a historically low level of 1.5% for the next 75 years.

Why is productivity growth important for the financial future of Social Security? Productivity measures the quantity of goods and services that can be produced with a given amount of labor, usually over one hour. If productivity increases, it means that we have become better at what we do by producing either more or better goods in the same amount of time. As we become more productive, our economic pie increases. This pie is then shared by giving more to workers in the form of higher wages and more employment, to companies in the form of higher profits, and to

"Productivity growth matters for Social Security because it raises wages and employment."

Figure 1



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consumers in the form of lower prices. Productivity growth matters for Social Security because it raises wages and employment.

With improved wages and employment, Social Security revenues increase. By multiplying wages and employment we arrive at the total wage bill for an economy, which incidentally is also the tax base for Social Security (with some minor modifications). Thus, as wages and employment increase, so does the tax base, and subsequently, with a constant tax rate, so does the revenue to Social Security.

"The trustees appear to create a Social Security shortfall by simply ignoring the fact that productivity growth could be and has been faster than they are willing to consider."

The importance of faster productivity growth for the financial future of Social Security is also reflected in the trustees' report. In their intermediate scenario, which puts the first year of the Social Security shortfall at 2038, the trustees assume that productivity will grow at 1.5% per year. In their more optimistic scenario, productivity will increase at 1.8% annually, which automatically translates into faster wage and employment growth. Consequently, the more optimistic scenario shows that Social Security never has an income shortfall. Instead, Social Security continues to accumulate assets through 2075, at which point it will own $15.4 trillion in today's dollars.

The real issue lies in deciding what a realistic future rate of productivity growth will be. To decide on a basic assumption like this, most economists let the past be their guide. To be prudent, however, economists look at both the more recent past, say, the last 20 years, and the more distant past, e.g., the past 40 years. The rate we should assume for the future should probably lie somewhere in the middle.

Using a procedure that gives equal weight to the more recent and to the more distant past is warranted by the roller coaster ride that annual productivity growth has been on for the past several decades. Productivity growth was above 2% and often above 3% in the decades following World War II. However, in the 1970s, following the oil price shocks, productivity growth slowed to a crawl, with average rates close to 1%. The productivity slow-down appeared to be reversed by the widespread implementation of new technologies in the late 1990s, when productivity growth again exceeded 3%. In other words, nothing says that low productivity growth cannot be reversed.

Given our past experience, a prudent assumption for productivity growth seems to lie close to 2%. Since 1947, annual average productivity growth was 2.2%. For the past 40 years it was 2%, and for the last 20 years it was 1.8%, but during the most recent 10 years it was 2% again. If we averaged the experience of the past 20 years and the past 40 years, average productivity growth would equal 1.9%. If we instead averaged the experience of the past 50 years and the last 10 years, average productivity growth would equal 2%.

No matter how we look at it, a reasonable productivity growth assumption for the future should be close to 2% — if we let the past be our guide to the future. However, the trustees assume lower productivity growth rates in both their moderate and their more optimistic scenarios. What may seem like small differences can generate large differences since the effect of slower or faster productivity growth is compounded year by year for the next 75 years.

In the latest trustees' report, the annual average rate of productivity growth from 1959 to 1999 is put at 1.8%. The average productivity growth rate for shorter, 10-year periods fluctuates in the trustees' calculations from 1.3% to 2.6%. While these numbers speak for making 1.8% a moderate assumption, the trustees consider it the most optimistic scenario. Put differently, the trustees appear to create a Social Security shortfall by simply ignoring the fact that productivity growth could be and has been faster than they are willing to consider in even their most optimistic scenario. Considering the importance of productivity growth for Social Security's finances and the prominence the trustees' report receives in the public debate, the trustees' decision to ignore the past is simply irresponsible. ❖

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Should We Privatize Social Security?

By
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University of
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President George W. Bush and the Republican-led House of Representatives want to privatize Social Security. The obvious question is whether this is a good idea for America. The more subtle question is just which Americans would it be good for—young workers or older retirees?

The problem with Social Security is that it is not a true pension plan but rather a "pay as you go" system. In true pension plans such as 401(k)'s and Individual Retirement Accounts, workers pay into a fund, the monies are invested in financial assets like stocks and bonds, and the size of the worker's retirement benefits is ultimately determined by the success—or failure—of the investments.

That's not how Social Security works. In today's "pay as you go" system, workers do pay taxes into the fund. But these revenues are simply used to pay the benefits to those currently retired under the system. Moreover, any surplus revenues are not put into any real investment accounts for workers. Instead, they are simply used each year to help balance the broader federal budget.

Such a "pay as you go system" has worked for more than 70 years for one simple reason. There have been plenty of workers to pay the taxes necessary to support the retirees. Indeed, every year the system enjoys a healthy surplus.

Now, however, the "graying of America" threatens the stability of Social Security. While there used to be as many as 16 workers for every retiree, that ratio has shrunk to about 3 to 1 and continues to fall. And therein lies the rub.

At present tax rates, the Social Security system will begin to run a deficit in 2016 because more money will be flowing out to retirees than coming in from worker taxes. As a result of this negative cash flow, the system is projected to be broke by 2038. So what's a President and Congress to do?

Of Politics and Ideology

One option would be to simply cut benefits. But that would be tantamount to political hara-kiri because a highly disproportionate share of the electorate is at or near retirement age.

A second option would be to simply raise the Social Security tax. That has little political appeal either—workers vote too—but it might also be economic suicide. The road to economic prosperity in America has never been paved with an ever-larger tax burden on American workers.

Still a third option would be to use any federal budget surpluses that are generated to square the Social Security accounts and put it on a firmer financial footing. This was the option favored both by President Bill Clinton and his would-be successor Al Gore. But two things happened on the road to using the budget surplus as Social Security's savior.

First, George Bush beat Al Gore—at least partly on a platform of privatizing Social Security. Second, and perhaps much more pertinent, the vaunted federal budget surpluses that were projected just a few years ago have now disappeared into a potential sea of red ink. How did this happen?

Part of that surplus was used by President Bush to fulfill another, much more salient political promise to cut taxes. More worrisome, future projected budget surpluses have potentially disappeared in an increasingly troublesome sea of economic recession.

Due to the prospect of a significant reversal of our budgetary fortunes, the smart political money is now betting that President Bush's bid to privatize Social Security will be dead on arrival. But that hasn't stopped the President from forming a bipartisan commission to explore the issue.

This commission is chaired by former Democratic Senator Daniel Patrick Moynihan and AOL-Time Warner exec Richard Parsons. It is expected to issue its report in November.

Critics of this commission say the commission is stacked with right wing, pro-privatization members. They warn that any report will be a whitewash on the issue.

Only time will tell. But to evaluate this issue and the commission's findings, let's review the major pros and cons of privatization.

Pros and Cons of Privatization

The first important thing to note about the Bush proposal is that it recommends only a partial privatization of the system. Under the working model, younger workers would be able to divert a percentage of the 7.65% in taxes they now currently pay into Social Security—perhaps a third—into a "personal retirement account" or PRA. Workers could then invest this money in the stock market in much the same way they do now with their IRAs and 401(k) plans.

At a macroeconomic level, the primary benefit of such a system is that it would turn what

"The graying of America threatens the stability of Social Security."

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is essentially now a "social insurance" program into a true pension plan. Supporters argue that this would provide much more stability to the system.

At the individual level, a second benefit would be to give workers more individual choice and responsibility in their retirement plans—an important goal of ideological conservatives.

"Critics maintain that privatizing the system would merely hasten the day of reckoning when the system goes broke."

Perhaps more to the economic point, such an approach would arguably also increase Social Security benefits to workers. This is because workers presumably would be able to earn a higher rate of return in the stock market than currently offered by the existing Social Security system.

In this regard, the average return for an all-stock portfolio over any 35-year period during the last 128 years has been at least 6%. In contrast, the implicit rate of return to workers paying taxes into the Social Security fund today will likely be less than 2%.

These arguments in support of privatization paint a picture of a more stable system with higher benefits for younger workers. So where, in the minds of critics, does the Bush proposal go so very wrong?

The first problem is that of the "transition gap." It goes to the very root of the "pay as you go" problem. To make the transition to a true pension plan, the federal government would have to start draining dollars out of the pay as you go system. But this would begin happening at precisely the time when there are too few worker tax dollars to begin with.

That's why the recently enacted Bush tax cut figures so prominently in the privatization debate. Without that $1.35 trillion tax cut, the budget surplus could have been used to bridge the transition gap. But with that surplus gone, critics maintain that privatizing the system would merely hasten the day of reckoning when the system goes broke. Indeed, at least one study has shown that taking just 2% of the 7.85% Social Security tax for Private Retirement Accounts would put the Social Security system in a deficit position as early as 2007 rather than 2016.

The second, perhaps even more telling, criticism of privatizing Social Security is implicit in this stark statistic: Over the last year, American investors have lost more than $5 trillion of wealth in the stock market—an amount equivalent to about half of the nation's gross domestic product.

The obvious concern here is that left to their own investment devices, many American workers might not actually boost their retirement benefits through prudent and profitable stock market investments; rather, they may simply get taken to the cleaners by the Wall Street pros.

In this regard, it is interesting to note that much of the political impetus for the privatization movement—as well as funding for much of the pro-privatization research—comes from Wall Street. This should hardly be surprising. Wall Street's financial sector stands to profit handsomely from a share of the more than $500 billion in Social Security taxes collected each year.

Yet it should also be noted that with about half of all American households now investing in the stock market, there are many young workers who would love to take their retirement destiny into their own hands with a self-managed investment portfolio.

Still, according to at least one study by Temple University's Jack Van Derhei, "most individuals lack all but the most basic knowledge of investment options and are unaware of what different investments might return." The other problem cited by the study is the "extremely optimistic expectations" that many investors have formed after watching the huge stock market run-up in the 1990s.

Certainly, with the Social Security system facing a grave challenge ahead, this will be a policy issue that will be talked about for years to come. That's why many Americans will cautiously await the findings of the Bush Commission. ❖

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Long-Term Care

By
Anne M. Wilkinson, Ph.D.
RAND Corporation

Although elderly Americans have what essentially is universal health care coverage under the Medicare program, elderly individuals who need long-term care are much less well protected.[1] Medicare covers many of the costs of acute medical care but only tangentially covers some long-term care services. Medicaid, the federal/state health program, covers long-term care but only for people who are poor or who become poor through paying for long-term or medical care. Who qualifies for Medicaid coverage varies from state to state, and people who need long-term care often do not get the care they need or prefer. For example, one of five adults with long-term care needs who lives in the community reports an inability to get the care needed.[2] Moreover, families' caregiving and financial burdens are often heavy because family and friends in the community provide most long-term care support.

What is Long-Term Care?

Long-term care goes beyond medical and nursing care to include all the assistance elderly persons would need if they needed assistance to perform basic tasks of everyday life for an extended period of time due to a functional disability or a chronic illness. Long-term care covers a diverse array of services including home health care, friendly visitor programs, home-delivered meals, chore services, adult daycare centers, respite services for caregivers, care management and social services, and assistive technology. Formal long-term care refers to a range of health care and supportive services provided by individuals and organizations paid to provide such care. Informal care refers to care provided on an unpaid basis by family members and friends.

Who Needs Long-Term Care?

The American population is growing older and those over age 85 comprise the fastest growing segment of the population. Those over age 65 account for 13% of the total population; nearly 6% of this total is age 75 and older and 1.4% is 85 and older. By 2030, when the entire baby boom cohort has entered old age, about 20% of the population will be over 65.[3] The older the person, the higher the probability that he or she will have disabilities. Persons turning 65 can now expect an average of 5.3 years of dysfunction characterized by acute or chronic illness.[4] Nearly one-quarter (22.9%) of all people aged 65 and over are functionally disabled or currently in need of some form of long-term care. It is estimated that by the year 2040, the population of severely disabled elderly will increase by 90%.[4]

Approximately 43% of people 69 and over will enter a nursing home at least once in their life.[5] However, the odds of entering a nursing home and staying for longer periods of time increase with age. Statistics show that at any given time, 22% of those age 85 or older are in a nursing home. Moreover, because women generally outlive men by several years, they face a 50% greater likelihood than men of entering a nursing home after age 65.[6]

What Does Long-Term Care Cost?

Long-term care can be very expensive. Nationally the average annual cost for a nursing home is more than $40,000 while a year of paid home care can average between $10,000 and $25,000. These amounts far exceed the financial resources of the typical elderly couple. Data from the Census Bureau suggests that the median income for a household over age 65 was $21,000 in 1999 and that less than half of households over age 75 have non-housing assets sufficient to cover one year in a nursing home.[7] Long-term care, along with prescription drugs, constitutes one of the two main sources of catastrophic health care costs for the elderly.[8]

Who Pays for Long-Term Care?

Generally speaking, the people who need the care pay the bills. Neither Medicare, nor private Medicare supplemental insurance (e.g., Medigap policies), nor the health insurance paid for by the elderly or by an employer will pay for long-term care. While "Medigap" insurance helps cover some of the gaps in Medicare coverage, those gaps are related to medical care services (e.g., hospital deductibles, doctors' deductibles, and insurance co-payments) but these are not long-term care services. The primary sources of financing for long-term care are Medicaid and out-of-pocket spending. Total nursing home and home care expenditures in 1998 were $150 billion. Medicaid and out-of-pocket costs account for the largest shares of total expenditures for long-term care. Medicaid paid 40% of these costs, families paid 26% of these costs out-of-pocket, Medicare paid for another 20%, private insurance paid 8%, and all other

"Women . . . face a 50% greater likelihood than men of entering a nursing home after age 65."

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sources (e.g., Veterans Administration, Administration on Aging programs, etc.) paid 7%. Two-thirds of long-term care spending was for nursing home care, 44% of which was funded by Medicaid, 14% funded by Medicare, and 31% paid for through out-of-pocket spending, private insurance paid 7%, and all other sources paid 5% of expenditures.[1]

"Approximately 75% of all caregivers of older persons are women (spouses, adult daughters, etc.)."

Thus states, through their state Medicaid programs, bear substantial responsibility for long-term care. Although coverage for home health services is mandatory under the Medicaid program, (Medicaid expenditures for home health services totaled $2.2 billion in 1999), states have two options in the way they can pay for other home and community-based services.[9] States may choose to cover services under one or both options: the personal care services program and the home and community-based waiver program. Under the home and community-based waiver program, states may request Health Care Financing Administration (HCFA) approval to cover non-professional services such as personal care, homemaker/chore services, home-delivered meals, adult day care, habilitation services, or any other services the state believes are alternatives to institutional care for their Medicaid populations. These "waiver" services need not be offered statewide and they may be targeted only to certain populations (e.g., elderly/disabled, persons with MR/DD, ventilator-dependent children, etc.). All states (including California) have at least one Medicaid-funded home and community-based waiver program.

Under the personal care services program, personal care services may be provided as an optional benefit under the state plan and only to cover personal care services. As contrasted with the waiver program, personal care program services must be made available statewide and must be provided to all Medicaid eligibles that meet need criteria. While the benefit is available to all those enrolled in the states' Medicaid program that meet the criteria for personal care, states may set coverage limits and these limits may be imposed regardless of need. States are under no obligation to provide the full amount of personal care services that disabled Medicaid-eligible individuals may require in order to have all of their needs for assistance met. Nor is a state required to provide a sufficient level of personal care services to ensure that recipients can live safely in the community. Thirty states (including California) and the District of Columbia include a personal care services benefit in their Medicaid programs.[9]

Nationally, 18.2% of long-term care spending for the elderly and disabled was for home and community services in 1999; $10.6 billion was for the waiver programs and $3.5 billion was for the personal care programs. However, there are dramatic differences across states and by target populations in what community-based services are covered. For example, Oregon spends 45% of its total long-term care expenditures for the elderly and disabled on home and community-based services while Tennessee spends 97% of its elderly and disabled long-term care expenditures on nursing homes.[9]

Informal Caregiving

The fact that more than a quarter of long-term care costs are paid directly by patients and families reflects the financing structure of long-term care; e.g., the absence of an insurance system, public or private, that spreads the financial risk of needing long-term care, and in its place, a system that protects people only if they are impoverished.[1] Given the high costs of long-term care, persons needing to purchase long-term care face a substantial financial burden.

However, out-of-pocket expenses for long-term care are only part of the picture of the burden for families. Family and friends provide approximately 70% of all long-term care for the elderly.[10] Family caregivers have always been the underpinning of long-term care for older persons in this country. There were 7 million people providing informal care to 5.2 million older people with disabilities living in the community (at least one functional limitation in ADLs (Activities of Daily Living) in 1998.[11] Informal care is the physical and emotional assistance to older relatives that makes it possible for them to remain at home. Among non-institutionalized elderly persons needing assistance with activities of daily living (ADLs), 65% depend solely on family and friends and another 30% supplement family care with services from paid providers. Only a little more than 5% rely exclusively on paid services.[11] The average length of time families provide such informal care is approximately 5 years.[12] If those persons needing assistance at age 50 are included, nearly 25% of all households have at least one adult who provided care.[13]

Approximately 75% of all caregivers of older persons are women (spouses, adult daughters, etc.).[12] While the average age of caregivers is 45, half of all primary caregivers are 65 or older and slightly over one-third are between the ages of 45 and 64. Over 66% of primary caregivers live in the same household with the older person for whom they provide care.[14]

The incidence of caregiving among Asian-Americans, African-Americans, and Hispanic households is higher than in the general population. In addition, the number of minority family members involved in caregiving is higher than those in non-minority families, particularly among adult children.[11] If the work of these informal caregivers had to be replaced by paid home care, the cost would range from $45 to $94 billion per year.[12]

Each older person with disabilities who lives with others receives an average of almost 30 hours of unpaid caregiving per week. As disability increases, elders receive more care. Those who are at greatest risk of nursing home placement receive about 60 hours of informal care per week.[14] In addition, caring for an impaired older person often requires physical demands, e.g., heavy lifting and turning, frequent bedding changes, and helping the person with toileting, all tasks which physically strain caregivers, especially those who are elderly themselves. Moreover, bearing the long-term care responsibilities for an older relative or friend with disabilities places terrible emotional strains on the caregiver and often results in depression. These strains can lead to restrictions on contacts with friends, neighbors, and other social contacts in the community.

Future Directions

As the Baby Boom generation nears retirement and old age, concerns about how the United States will meet the long-term care needs of its growing elderly population are intensifying. In the absence of a public long-term care financing and delivery system or widespread private long-term care insurance coverage, the main source of long-term care assistance for the majority of disabled elderly living outside of nursing homes has been unpaid family members and friends and state Medicaid programs.[15] Research has shown that the degree of caregiver involvement in long-term care has remained fairly constant over more than a decade, bearing witness to the remarkable resilience of the American family in taking care of its elders.[14]

However, the projected steep increase in the elderly population coupled with the upward trend of more women entering the workforce (thus reducing the availability of family caregivers) means there will be a greater reliance on the use of formal long-term care services in the future. Indeed, the use of formal long-term care services is already increasing. The percentage of disabled elderly persons using formal long-term care services, funded by both Medicare and Medicaid, increased between 1982 and 1994. Out-of-pocket payments for long-term care also increased.[15] Moreover, the decline in fertility of the Baby Boom cohort implies that there will also be fewer children per elderly person potentially available to provide care. President Clinton's proposal for a modest tax credit for severely disabled persons and their caregivers in addition to federal grants to the states for caregiver services is evidence that there is a public interest in the burden of long-term care on families. All the same, trends in financing of long-term care, for example, the limitations in funding home health care by the Medicare program, mean that more costs for long-term care will fall on state Medicaid programs. Limitations in the Medicaid program coverage (e.g., low income requirements) and variability of levels of funding for community-based services across the states suggest that access to care will be negatively affected and that many more elderly individuals' needs will go unmet.

This brief discussion has highlighted some of the issues policymakers continue to face regarding balancing between nursing home and home care, assuring quality, integrating acute and long-term care, and providing affordable access to long-term care services. Some state models of care have been able to address the desire for the elderly to remain in the community and to reduce nursing home use (e.g., Oregon). However, the success of the program has required not only limits on nursing home use but limits on the availability of home care (resulting in waiting lists for care).[1] The challenge of the future will be to devise a system of long-term care that can spread the costs of long-term care rather than concentrating them in either the Medicaid program or from families and patients themselves. ❖

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"Bearing the long-term care responsibilities for an older relative or friend with disabilities places terrible emotional strains on the caregiver and often results in depression."

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Women's Retirement Security

By
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Women's lives are getting better and worse. On one hand, women have equal rights to jobs, education and property, and more women are working for pay than ever before. Yet women stand alone in enduring high rates of poverty in old age. Why? The answer lies in both marriage and work. How women and men approach paid work, how the labor market treats them, and how wives and husbands spend and save in today's marriage affect who gets what in old age.

The good news is that the elderly can afford to eat less dog food than they did 30 years ago. The poverty rate among Americans age 65 and over has fallen from 35.2% in 1959 to 10.5% today.

The bad news is that one out of five elderly women is poor, and an elderly woman's chance of falling into poverty increases fourfold if she does not have a husband. The poverty rate for elderly married couples is less than 5%; for an elderly single woman, the chance of being poor is over 22%. In 1997, the median income for elderly unmarried women (widowed, divorced, separated, or never married) was $11,161, compared with $14,769 for elderly unmarried men and $29,278 for elderly married couples.

American elderly have four main sources of income: (1) mandatory and nearly universal Social Security; (2) voluntary employer-based pensions; (3) private wealth; and (4) continued work. (The U.S. stands apart from other nations in making mandatory retirement illegal.) Welfare is a small part of retirement income, and the unpaid care provided by adult women for their elderly parents is an unmeasured asset.

Social Security

The U.S. Social Security system, as in most countries, is progressive: it provides higher replacement rates for lower-income workers. The program is not means tested, meaning that contributors with similar work histories get similar benefits even if one has a large amount of wealth. Non-married older women receive 51% of their retirement income from Social Security because of the progressive formula, the subsidy to dependents, and the cost-of-living annual adjustments (which help those who live longer than the average beneficiary). Couples, in contrast, receive less than 36% of their income from Social Security.

Voluntary Employer-Provided Pensions

Pension coverage and generosity vary greatly between occupations, employers and industries. Less than one-half of American workers have employer-based pensions, and women's pensions are half the value of men's. Women receive approximately $3,000 per year. While almost 20% of married couples' income comes from employer-based voluntary systems, only 15% of single women's income comes from employer pensions. This low rate stems from low pension coverage, inferior pensions, and inadequate rules about survivorship and divorce. Women get smaller deferred-wage pensions because of their situational choices and the limitations they face early in their lives. Also, the trend toward 401(k)'s and defined-contribution pension plans and away from traditional defined-benefit principles is more dangerous for women. Women are better off having group-based annuities offered under defined-benefit plans and Social Security. And all people who live a long time after retirement especially need inflation-protected annuities. So, despite some complaints about so-called gender inequities in Social Security, the program's defined benefit, price indexing, and redistributive role are necessary to keep large numbers of older women (and minorities) out of poverty.

Assets

Elderly married couples obtain 18% of their income from assets; for unmarried women, the figure is 20%. Older women's living standards suffer in the absence of husbands, and they also may suffer because of husbands. Our system of individual-based pensions and retirement accounts requires retired couples to go beyond human capacity to foresee the future to protect a surviving spouse against poverty. A newly retired couple may move to a warmer climate, travel, and do all the things they couldn't do while they both worked and raised children. The problem is two-fold: these activities deplete savings, and husbands are more likely to die before their wives. Wives would have to speak up and declare the unthinkable—that their husbands will probably die before them—and, after this Herculean statement, assert that he should have less so she can have more income security later. Power relations in marriages are beyond the scope of this discussion, but note that the problem lies in the United States' significant dependence (relative to other nations) on individuals having accounts serving

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insurance purposes. Social Security insurance (which is inflation indexed) and defined-benefit annuity payments (an annuity is a stream of income payable for life) somewhat lessen this dependence and provide insurance against "living too long" by delivering an insurance base.

Rules about survivors' benefits and divorced women's benefits, as well as these consumption patterns that are biased for husbands, also boost poverty rates for single women. Divorced women's access to pensions depends heavily on their lawyers' abilities and particular state laws. Consequently, only 27% of divorced women collect pensions from former spouses.

"Older women workers are more likely than older male workers to be clearing tables at fast food joints."

Continued Work

The fourth source of income is the old-fashioned source—paid work. Although the labor force participation of American women has increased rapidly, elderly couples benefit from men working. Elderly couples get a full fourth of their income from earnings, while unmarried older women get only 10% of their income from earnings. This makes sense. Women have worse jobs than men. Because age discrimination is illegal, many older Americans work. Unfortunately, older women workers are more likely than older male workers to be clearing tables at fast food joints.

Specific Ways to Help Women In Retirement

There is no such thing as a bundle of reforms that are "good for women" or "bad for women," because there is no such thing as a representative older woman. Socio-economic position is as important as gender in explaining retirement income security. Despite the difficulty in generalizing, I propose the following policies to help women gain retirement income security.

Recommendation 1:

Modify 401(k) rules so that the tax advantage applies only if the employer enrolls all eligible employees in the plan and provides a minimum contribution (perhaps 1 - 3%) for all employees. Employees may opt out only if they sign an informed consent form. This helps workers not have to choose between savings and needed income. The McDonald's Corporation has default enrollment and participation, especially among women, is much higher than at the average low-paying firm.

Recommendation 2:

401(k) rules should be updated to include the same spousal protections that are in defined-benefit and defined-contribution rules. The Retirement Equity Act of 1984 requires spousal consent for pension distributions other than joint and survivor options.

Currently, pensions enter into divorce settlements as property. Because women more often than men face financial difficulties in divorce, wives are likely to choose cash over pensions in the settlement. Moreover, valuing pensions is difficult for most lawyers and entails considerable expense.

Recommendation 3:

If all divorce decrees provided, as the default, that one-half of the marital share of the participant's accrued benefit was given to the former spouse, more wives would likely collect. In a closely related proposal, the Department of the Treasury could publish model spousal consent forms for 401(k)'s and qualified domestic orders, in order to spare individuals the expense of having a lawyer determine the pension value.

Recommendation 4:

Workers on parental leave should be able to make up missed pension contributions and service by buying back service credit (more boldly, employers could be required to maintain contributions to pension and health plans while workers are on leave for parental duties). Many plans allow military time buy-back—a benefit that mainly helps men do non-market but important duties. (This proposal could very well be biased in favor of higher-income individuals, because they would be more likely to have the extra cash to

Table 1

Sources of Income to the Elderly: Percent of Total Income

	Social Security	Pensions	Income from Assets	Earnings	Other
Unmarried Women	51%	15%	20%	10%	4%
Unmarried Men	39	22	16	19	4
Married Couples	36	20	18	25	1
All Elderly	40	18	18	20	4

Source: Social Security Administration, 1996 buy back service, especially around the financially stressful time of a child's birth; moreover, higher income individuals are more likely to take unpaid leave to care for children.)

Recommendation 5:

The Social Security formula should redistribute benefits so that a couple gets a little less and the survivor more. Couples get 150% of the worker's benefit when both are alive. Surviving spouses get only the worker's benefit, so that the income is 67% of what the married couple received. The official poverty thresholds imply that a widow or widower needs 79% of a couple's income to maintain consumption levels. Thus, a woman in a married couple who was just above the poverty line can fall below the line after losing her husband.

Recommendation 6:

Reinstate the Social Security minimum benefit that was eliminated in the early 1980s. Prevent the erosion of the Social Security benefits that may come out of partial privatization or cutting the Social Security cost-of-living annual adjustment.

Recommendation 7:

Women can help themselves by obtaining pensions, protecting pensions in divorce, and planning for widowhood by being in a stronger bargaining position *vis a vis* their spouses and employers during their working and married lives. Being in a union boosts women's chances of being in a pension by 50%—more, if the job is in retail—and getting equal pay will also help women get better pensions.

In sum, the idea that retirement income is based on a "three-legged stool" of Social Security income, employer-based pensions, and savings is inaccurate in describing older women's retirement income reality. Older women's retirement income is like a Social Security sheet cake with a thin layer of pension-plan frosting with sprinkles of savings and wages from low-paid work. The frosting is thicker while the woman has a husband, but it thins out when he is gone. Boosting Social Security benefits, expanding pensions in the retail and service sector, and raising wages are among the changes that will lower the risk of poverty for the nation's elderly women. ❖

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Beyond Social Security: The Local Aspects of an Aging America

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"We can already identify demographic trends that will prove challenging for the nation's regions."

The phrase "demography is destiny" underscores the national impact of America's large and growing elderly population. Medical breakthroughs and other lifestyle and social changes over the course of the 20th Century ensure a longer life expectancy among Americans surviving into the 21st Century. This increased longevity is especially important because of its compounding effect on the large post-World War II baby boom cohort—76 million strong—as its members begin entering elderhood around the year 2011. From birth to the present, the baby boomers have pushed their way through the nation's school systems, labor market, housing market, and stock market—transforming institutions, both public and private, in their wake. The social and economic impacts should be just as precedent-shattering as the baby boomers march, in large numbers, into their senior years. The national impacts this throng is bound to have on federal entitlement programs like Social Security, Medicare, and Medicaid have dominated policy discussions of their demographic destiny. Yet, the current policy emphasis on future impacts of baby-boom aging for programs administered by the federal government overlooks the demographic divisions within today's elderly population, which hold local implications for central cities and suburban communities.

For particular segments of the older American population, where they live matters. Older Americans differ in health, wealth, ethnicity, race, and age. Some regions of the country, specific metropolitan areas or retirement communities, are able to attract the "demographically advantaged" segments of the senior population: well-educated "young elderly" and married couples in good health, with high disposable incomes and low demands on public services. Yet, relatively few of these retirement haven areas exist. The senior populations in most communities arise simply because life-long residents "age in place," which means that the social divisions that exist across space for the entire resident population become perpetuated and even exacerbated among the elderly population. Fast-growing regions in the nation's sunbelt that attracted professional, well-educated workers during their pre-elderly years will inherit a more "demographically advantaged" aging-in-place senior population. Similarly, suburban communities that attracted upper- and middle-income families in the middle stages of their life course will find themselves with elderly residents who will contribute more to the community's tax base than they take away.

In contrast, central cities, inner suburbs, and metropolitan areas in regions that have suffered economic and demographic declines in recent decades will continue to house disproportionate numbers of the nation's "demographically disadvantaged" elderly - "older elderly" people, widows and widowers, female-headed households, those with incomes below or near the poverty level and relatively high levels of disability, and (in central selected cities) significant low-income minority populations - as they continue to age in place. Concentrations of older, economically vulnerable, and disability-prone populations pose special challenges for local institutions as well as city and county governments that are often the most financially strapped.

Looking ahead to the coming "age wave" as baby boomers march into their senior years, we can already identify demographic trends that will prove challenging for the nation's regions, cities, and suburbs. For the mass of aging boomers, the "aging-in-place" phenomenon will prevail, and create even sharper social divisions across communities than is the case today. Boomers are much more divided with respect to marital and living situations, the presence or absence of children who can provide support in old age, and

Table 1

Percent Poverty, Household Income, and Homeownership of U.S. Elderly Households, 1997 (a)

	Poverty Rate	Percent Income More than $25,000/year	Percent Homeowner
Household Type			
Married Couple	4.5%	45.4%	91.5%
Male-householder Family	9.1%	47.4%	77.8%
Female-householder Family	14.1%	30.4%	78.6%
Male-headed nonfamily	13.3%	20.8%	66.2%
Female-headed nonfamily	23.0%	12.2%	67.7%
Total	10.8%	33.9%	82.1%

(a) For households with householder age 65+.

Source: Author's analysis of Current Population Survey Data.

access to wealth and private pensions than today's elderly were during their working years. Moreover, because the plurality of boomers have lived most of their lives in the suburbs, distinctions between "have" and "have-not" communities will not cut across the city-suburb dichotomy. Concentrations of "demographically disadvantaged" elderly boomers will arise within suburban communities that will not be prepared to deal with the social services, health care, and transportation needs of a fast-growing, less-well-off senior population. These places will become common within most of the nation's metropolitan regions.

Many of these disparities in poverty, income, and assets play out across different types of households. Married-couple elderly households, especially those in the 65-74 age group, have the lowest rates of poverty and the highest rates of home ownership, and high levels of annual income (see Table 1). The households that fare the worst are women living alone or with non-relatives (female-headed non-families.) Still, home ownership among the elderly is relatively pervasive across all household types, indicating that a house can serve as an important asset for households with low incomes or without other financial resources.

Elderly Divisions: Regions, Cities, and Suburbs

The geographic distribution and spatial shifts of the elderly population will become more important as the elderly become a larger share of the national population. Regions and communities that tend to retain or attract more demographically advantaged segments of the elderly population will see a rise in the consumption of local services, net gains to their community tax bases, and the involvement of an energetic, active population. On the other hand, areas that tend to keep the less advantaged segments of the elderly will need to provide greater community services and expect net losses to their tax bases.

It is important in examining elderly population redistributions to not overemphasize the role of elderly migration. Typically, the elderly migration rate is small compared to the whole population. In any given year about 20% of working-age Americans make a residential move. By contrast, only 6% of the elderly relocate, and most of these moves are local. Slightly more than 1%of the elderly population moves into a different state in any given year. The migration of the elderly is important for specific "retirement magnets" - states, communities, and regions that have special attractions for elderly residents. Small migration streams of elderly from a variety of places descend upon a small number of destinations where their impact is significant. However, on the whole, the growth or decline of the elderly population in most communities is less reliant on migration than the simple aging-in-place of existing residents.

Elderly growth results from substantial aging-in-place while, in retirement magnet areas, migration tends to be associated with demographically attractive segments of the elderly population. Migration tends to select on the "best and brightest" of the resident population. In other words, those who move tend to be those with the most resources. By far,

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Table 2

Regional and Metropolitan Distribution of Elderly and Non-Elderly Population in U.S., and Change, 1980-1997

	1997 Distribution			1980-97 Percent Change (a)			Percent 65+ Within Area	
	Elderly	Non-Elderly	Difference*	Elderly	Non-Elderly	Difference*	1997	Change since 1980
NORTHEAST								
New England	6%	5%	1%	23%	6%	17%	14.0%	1.7%
Mid-Atlantic	16%	14%	2%	20%	2%	18%	14.2%	1.9%
MIDWEST								
East North Central	16%	16%	0%	25%	3%	22%	12.8%	2.0%
West North Central	7%	7%	0%	15%	7%	8%	13.6%	0.8%
SOUTH								
South Atlantic	19%	18%	1%	51%	28%	23%	13.7%	1.9%
East South Central	6%	6%	0%	24%	10%	14%	12.6%	1.3%
West South Central	9%	11%	-2%	32%	24%	8%	11.0%	0.6%
WEST								
Mountain	5%	6%	-1%	76%	42%	34%	11.3%	2.0%
Pacific	14%	16%	-2%	49%	33%	16%	11.3%	1.1%
TOTAL	100.0%	100.0%		33%	16%	17%	12.7%	1.5%
Large Metro	51%	55%	-4%	34%	19%	15%	11.9%	1.2%
Small Metro	26%	25%	1%	45%	17%	28%	13.0%	2.2%
Non-Metro	23%	20%	3%	21%	8%	13%	14.6%	1.4%
TOTAL	100.0%	100.0%		33%	16%	17%	12.7%	1.5%

(a) = [(1980-1997 Elderly Change) x 100]/(1980 Elderly Population) ***Elderly minus Nonelderly**

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the largest elderly migration flows are made up of educated, relatively well-off, young-elderly married couples. Aging-in-place will always result in a growing elderly population when the number of persons entering into elderhood—turning age 65 in any given period—exceeds the number of deaths and move-outs. Aging-in-place is fairly pervasive, especially during periods when there is a large throng of those about to enter their elderly years. It will be especially common after 2011, when the baby boomers—located in all parts of the country—begin turning 65. In contrast, only a small number of areas have recently experienced an elderly population decline due to greater elderly out-migration and mortality than aging-in-place. These tend to be rural areas that have not grown for many years, and, less commonly, central cities whose populations are declining severely.

"The elderly tend to be over-represented in the Northeast and the South Atlantic portion of the South."

Migration selectivity is also relevant to the contributions of the aging-in-place population. Regions and communities with large soon-to-become elderly populations are the areas that successfully attracted large numbers of migrants with "good demographics" during their working years. These areas tend to be located in growing parts of the country such as the Sunbelt and in growing parts of metropolitan areas - typically seleted suburbs.

Regions and Metropolitan Areas

The current distribution of the elderly population across broad regions and metropolitan areas of the United States does not differ that much from the rest of the population. Most elderly and non-elderly people tend to live in the Sunbelt, especially the South Atlantic part of the South, and both tend to live disproportionately in large metropolitan areas - those with populations exceeding one million. Compared with the younger population, the elderly tend to be over-represented in the Northeast and the South Atlantic portion of the South.

The Northeast's elderly representation is essentially a remnant of the past since this region's non-elderly population has in recent decades been more likely to relocate to other regions. The South Atlantic elderly concentration, on the other hand, reflects the strong and concentrated elderly migration to this region, especially Florida. Across the metropolitan spectrum, the elderly in past decades have been more likely to either remain in or move toward smaller and non-metropolitan areas than the younger population.

The close alignment of elderly and non-elderly population distribution is due, in part, to elderly redistributions over the last two decades. The growth of the elderly population through both migration and aging-in-place has been greatest in the Mountain West and in the South Atlantic states. A warm climate, low cost of living compared to the Northeast and other urbanized parts of the country, and other amenities have helped to make these states especially attractive to seniors. In contrast, a good part of the West, Midwest, and Northeast have exhibited the slowest elderly gains.

A useful statistic for showing the prominence of the elderly population in an area is the percentage of the population composed of elderly people. When examining this statistic, one should be aware that a high "percent elderly" does not necessarily suggest an attraction for elderly migrants or large aging-in-place population. It might simply indicate that there has been a long-term out-migration of the younger population, leaving disproportionate numbers of the less-mobile elderly behind. This is the case for a large part of the nation's mid-section, ranging from North Dakota southward through Oklahoma and Arkansas, as well as for a broad swath of the Northeast.

Just as with states, metropolitan areas that have shown the greatest elderly growth since 1980 are located in the Sunbelt. Among the nation's largest metropolitan areas, Las Vegas, Orlando, and Phoenix had the largest increase in their elderly populations over the past two decades (see Table 4). Significant jumps in older American populations are also

Table 4

Metro Area with Greatest Elderly Growth, 1980-97

Large Metros Areas (a) with Greatest Growth			Small Metro Areas with Greatest Growth		
Rank	Area	Growth	Rank	Area	Growth
1	Las Vegas, NV-AZ MSA	258%	1	Anchorage, AK MSA	256%
2	Orlando, FL MSA	94%	2	Naples, FL MSA	201%
3	Phoenix-Mesa, AZ MSA	92%	3	Fort Walton Beach, FL MSA	194%
4	West Palm Beach-Boca Raton, FL MSA	88%	4	Ocala, FL MSA	183%
5	Sacramento-Yolo, CA CMSA	78%	5	Myrtle Beach, SC MSA	171%
6	Houston-Galveston-Brazoria, TX CMSA	72%	6	Melbourne-Titusville-Palm Bay, FL MSA	160%
7	Austin-San Marcos, TX MSA	67%	7	Fort Pierce-Port St. Lucie, FL MSA	147%
8	Jacksonville, FL MSA	66%	8	Las Cruces, NM MSA	131%
9	Raleigh-Durham-Chapel Hill, NC MSA	66%	9	Punta Gorda, FL MSA	129%
10	San Diego, CA MSA	63%	10	Jacksonville, NC MSA	120%

(a) Large Metro areas are CMSAs, MSAs, and (in New England) NECMAs with populations greater than one million: OMB definitions of June 30, 1995.

Source: Author's analysis of U.S. Census Bureau Decennial Censuses and Postcensal Estimate Data evident in metro areas in Florida, Texas, several Atlantic coastal states, and the Rocky Mountain states. Among smaller metropolitan areas, six of the top nine fastest-growing metro areas are in Florida, and there is a fair representation of other smaller eastern seaboard metros and communities in the West. These areas achieve much of their growth from in-migration of elderly as well as from aging-in-place. Some of these areas have attracted a significant number of residents in their 50s who relocated to these areas with an eye toward retiring there.

Two indicators of special interest involve the potential isolation of the elderly who eventually will be unable to drive and may experience mobility limitations. The suburban elderly in growing southern and western metropolitan areas appear to have the highest level of automobile ownership (in the suburbs of Phoenix, only 9% of the elderly do not own a vehicle). The suburban preference of the elderly in these growing metropolitan areas raises the question of whether they will still be able to function effectively when they reach the age when operation of an automobile may be difficult. In contrast, most of the older central cities with good public transportation systems are home to relatively high percentages of older Americans who do not own vehicles; in New York City, 63% do not do so. The issue of how well these suburbanites can cope as they age in place within more isolated suburban communities is of potential concern.

Implications for Cities and Suburbs

Not all elderly who age in place create problems for their local communities. Indeed, vast stretches of the Sunbelt have benefited greatly from aging-in-place because they attracted large numbers of professionals and high-income households during their prime labor force years and retained these people as they aged into seniorhood. Similarly, suburban communities on the outskirts of today's growing metropolitan regions benefit greatly by retaining middle- and upper-income suburbanites who age in place there. Yet in large parts of the Midwest and in many cities and inner suburban communities, one finds the aging-in-place of blue collar, less well-off elderly along with the "demographically disadvantaged" groups discussed above. These areas will require greater attention toward providing public services for their elderly populations. Moreover, as these elderly residents continue to age, their needs arising from failing health, death of a spouse, and increased disabilities will proliferate in communities that will not have the appropriate infrastructure.

As baby boomers age into elderhood, their local impacts on specific cities and suburban communities will be worthy of just as much attention as their national impacts on federal entitlement programs. The community contexts for baby boomers, with the exception of minority groups, will be largely suburban. Many of these will simply evolve as current communities "age-in-place" but there will also be a growth industry in the development of retirement communities designed to lure the better-off segments of these large boomer cohorts. The latter "yuppie elderly" will certainly be the target of localities in all parts of the country hoping to capture this demographically desirable group. Retirement communities will also develop within most metropolitan areas.

Thus, moreso than today's elderly, the aging boomers will live in suburban communities that will be unprepared to deal with the special needs of seniors. In their working lives, these households depended heavily on automobile transportation for almost all daily activities. This will be less the case as they age. Moreover, compared to today's elderly, the baby boomer seniors have fewer children and smaller kinship networks to rely upon for informal assistance in times of sickness or other special needs.

What remains to be seen is what happens to the segments of the baby boomer elderly with fewest resources and significant service requirements. This will be especially important during the third and fourth decades of the new century, as these populations become more dependent, while they continue to reside in the dispersed settlement systems of today's urban America. ❖

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"Needs arising from failing health, death of a spouse, and increased disabilities will proliferate in communities that will not have the appropriate infrastructure."

Table 5

Demographic Profile of Cities and Suburbs, U.S. Elderly, 1997 (a)

	Central City*	Suburbs*
Household Type		
% Married Couples	48.8%	59.3%
% Female-householder Family	10.8%	7.1%
% Female-head Nonfamily	27.9%	23.6%
Education		
% Less than High School	35.9%	28.6%
% High School Grad	64.1%	71.4%
% Some College+	31.7%	34.5%
% Poverty Households	14.0%	7.4%
% Household Income GT $25,000	33.0%	39.8%
Percent Homeowners	71.7%	84.6%

(a) Statistics for age, education pertain to persons age 65+; all other statistics pertain to households with householder age 65+.

Source: Author's analysis of U.S. Current Population Survey

Facts and Figures

Important Information About California